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SUBJECT: INDIA'S LOOK EAST ECONOMIC POLICY - JUST LOOKING, NOT  
BUYING

CALCUTTA 00000464 001.2 OF 004

¶1. (SBU) SUMMARY: India continues to adopt a contradictory attitude in its trade relations with its Eastern neighbors, claiming to seek more bilateral trade agreements but placing severe limits and barriers to those agreements to make them essentially meaningless. The opening on July 1 of Indo-China border trade at Nathu La was seen as an important initiative by India in strengthening regional trade as part of its much touted "Look East Policy." Subsequent developments indicate a continuing protectionist stance due to concerns over national security and the potential dumping of goods from China. A closer analysis of the trade relationship between India and its other neighbors also shows that fear of direct external competition continues to stifle India's "Look East Policy." Ironically, while the GOI criticizes developed countries for unfair trade practices against developing countries, India itself conducts highly discriminatory trade policies with other developing Asian countries. END SUMMARY.

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Trade through Nathu La Purely Symbolic  
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¶2. (U) On July 1, the opening of the Himalayan Nathu La trade crossing between India and China was heralded as a great leap forward in the trade relations between these two Asian giants. However contrary to the initial hype, India's restrictions on the type and number of commodities, a lack of unified standards for commodity inspection and quarantine, a limited trading time as a result of the climactic conditions, and bad infrastructure have ensured that the volume of trade through Nathu La remains low. For example, the GOI has limited items for trade to goods such as yak tail, yak milk and other esoteric products. The GOI has also imposed stringent quarantine provisions on these agricultural items. Currently, there are no provisions for obtaining a quarantine clearance on the border, so the paper work has to be done in Calcutta, compounding delays. The GOI

Commerce Ministry is examining alternatives to resolve the issue but has not reached a decision.

13. (U) Other administrative delays abound, such as requiring Nathu La traders to provide their income tax number (known as a PAN number), during transactions. This requirement caused long-holdups, as Sikkim residents were exempt from income tax requirements and did not have PAN numbers. The GOI has now removed this requirement for Sikkim resident traders. Trade is, however, curtailed by restricting the maximum value of each consignment to USD 555.

14. (SBU) In addition, the permitted trade list includes just 29 items for export and 15 items for import by India from China. The Sikkim government has submitted an application to the GOI urging it to expand the list, but the application remains pending with the Commerce Ministry. The Sikkim government would like to include, among other things, agricultural and horticultural products, including orchids. It has also urged the GOI to permit tourism sector operations through Nathu La. The GOI has shown little interest in opening the crossing to tourists. (Note: Contacts have told Post that during his recent visit to Gangtok, the Chinese Ambassador indicated that his government asked the GOI for an expansion of the trade list. End Note.)

15. (SBU) India's development of infrastructure on its side of the Nathu-La border lags behind China's. While international media have touted the development of rail and road access to Nathu-La on the Chinese side, the GOI and Sikkim government have so far only just decided to upgrade the road network from Siliguri (in West Bengal) to Nathu La. USD 111 million was allotted to upgrade the road between Siliguri and Sikkim's capital, Gangtok, so that it can support larger container trucks. The Border Roads Organization (BRO), an agency under the Ministry of Defense, builds and maintains this road. USD 44 million has been earmarked for upgrading the stretch between

CALCUTTA 00000464 002.2 OF 004

Gangtok and Nathu La. The work is projected to be completed by 2008. Assuming the road improvements happen, significant India-China border trade through Nathu La cannot be expected prior to 2009.

16. (SBU) Comment: India's historical distrust of China is a contributing factor in its hesitation to compete with Chinese products. The outcome of the 1962 Indo-China war and continued fears of border disputes remain etched on the Indian psyche. While the opening of the Nathu La border was portrayed as a warming of relations between the two nations, India's real achievement was China's final recognition of Sikkim as an Indian state in 2003. End Comment.

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The Imbalance with Bangladesh  
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17. (SBU) India's trade relationship with Bangladesh is also instructive of how India treats its South Asian neighbors. The trade imbalance between the two countries is sizeable. According to the Bangladesh Deputy High Commissioner (BDHC) in Calcutta, Bangladesh exports approximately USD 240 million to India, while India exports nearly USD 2 billion to Bangladesh. The BDHC noted that although overall exports to India have increased year-on-year, a series of non-tariff barriers continue to impede free trade into India. For example, cotton and silk saris must be checked for potential skin irritants. This process involves sending a sample of the material to Lucknow, a process that delays the imports by about three weeks. Indian law requires that a tax commissioner attest to imports coming from Bangladesh, but the tax commissioner has his office in Calcutta, not at the border. Some customs posts are unmanned. Customs officials capriciously apply tariffs and duties on goods, preventing uniformity. Like the Chinese experience with Nathu-La, infrastructure is much less developed on Indian side

of the border as compared to the Bangladesh side. India's restrictions on trade with Bangladesh have regional implications as well. Bangladesh and Nepal had entered into an agreement with India to permit transit of goods crossing a narrow strip of land in India that divides the two countries. However, there is little use of the route as Bangladeshi and Nepali trucks are not permitted in India. Goods therefore must be unloaded at the border and reloaded into new trucks just to travel the approximately 30 kilometers across India.

¶18. (SBU) Comment: The BDHC felt that India had little incentive to agree to a more liberalized trade regime with Bangladesh. For its part, the GOB does not press its case too hard with the GOI because it relies so heavily on Indian imports and because it feels that the GOI can affect the market price of basic foodstuffs. The BDHC cited as an example, the GOI stopping exports of onions and sugar to Bangladesh three months ago, ostensibly due to low domestic supply. This move was seen in Bangladesh, though, as the GOI reminding Bangladesh as to who controlled the market. End Comment.

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Stonewalling on Trade Pacts with Southeast Asia  
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¶19. (U) India has signed Framework Agreements with Thailand, ASEAN, Malaysia, Indonesia and Korea in hopes of achieving Comprehensive Economic Cooperation Agreements (CECA) in line with the CECA India signed with Singapore in 2005. The CECA, a euphemism used by the GOI for a Free Trade Agreement to avoid conflict with domestic anti-free trade lobbies, typically begins with just liberalized trade in a limited range of products.

CALCUTTA 00000464 003.2 OF 004

¶10. (U) The Indo-Thai Framework Agreement signed in October 2003 involves an FTA in goods, services and investment. After prolonged negotiations over rules of origin and a drawing up of lists for phased, tariff-free trade, a scheme listing 82 products allowed for trade began September 1, 2004. Tariff reduction was to be 50% for the first year, increased to 75% for the next year, with free trade in effect from September 1, 2006. Trade between the two nations is dominated by ten products. India's exports to Thailand include fuel, oil, precious stones, and electrical items, and in turn India imports chemicals, agricultural products, precious stones, machinery, plastics, spare parts, electronic items and auto components. The balance of trade was weighted slightly in India's favor in 2004-2005, but has since shifted in favor of Thailand in 2005-2006. Thai exports to India have increased by 1.7% in the last six months.

¶11. (SBU) The Framework Agreement further called for widening the free trade list, once the scheme got off ground. On April 12, Congress President Sonia Gandhi wrote to Prime Minister Manmohan Singh advising the government to "very carefully scrutinize" FTAs to protect farmers. A Thai Consul in Calcutta informed Post that this led to a delay in further negotiations; though, he hopes negotiations will be resumed after the mid-October elections when the political situation stabilizes in Thailand. Liberalizing trade in another 4,000-5,000 products and expanding cooperation in services and investment are some of the issues that will be discussed when talks resume. The deal is supposed to be expanded by 2007, since the rules of origin issues have been resolved and the primary focus would be to lower the number of items on the sensitive list. Post contacts note that Indian suppliers of agricultural products, small scale industry products, chemicals and electronics, fearing competition, have sought to block the GOI from opening these sectors to trade.

¶12. (U) Indo-ASEAN trade talks had also been stalled on the ground of India's "sensitivity" to further lowering the number of products on its exclusion list from its high of 1,414 items.

Negotiations took over a year just on items like toilet seats, dolls and chewing gum. Though India agreed to reduce the excluded items list to 850 products, Malaysia, the country coordinator and the chair of the trade talks, was not satisfied. Malaysian International Trade and industry Minister Datuk Seri Rafidah Aziz observed that the negotiations had become "difficult," since goods on the exclusion list accounted for 30% of ASEAN's exports to India.

¶13. (U) Malaysia wants the list to contain no more than 60 items. Malaysia and Indonesia are especially interested in market access for palm oil, which is included in India's negative list. Earlier, India had agreed to allow import of the commodity in limited amounts through tariff rate quotas. Malaysia had refused to accept the offer. India has now proposed to reduce the excluded items list to 560, while 294 items will continue to enjoy tariff protection for just five additional years. India has agreed to reduce duties on palm oil to 50%, refined palm oil to 60% and pepper and tea to 50% over a ten year period. The future of India-ASEAN CECA talks now depends on how ASEAN and in particular Malaysia reacts to India's offer. The implementation of the Indo-ASEAN FTA has already been delayed by over a year and both sides have dropped a proposed "early harvest scheme" program for immediate tariff cuts on specific products. The new deadline for the implementation of the FTA is January 1, 2007 - which is unlikely to happen. Malaysia too had called off its bilateral economic cooperation negotiations with India until it felt India was genuinely interested in trade liberalization.

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Domestic Interests Hamstring Further liberalization  
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CALCUTTA 00000464 004.2 OF 004

¶14. (U) In addition, Post's domestic industry contacts object to implementation of tariff concessions under the regional trade agreements (RTA). Indian industry complains that with products such as chemicals, electronic and auto components, the RTAs have resulted in finished products being imported at a lower duty than the related raw material inputs used for domestic manufacture. For example, the import duty on color televisions is 6.25%, but the duty on color tubes is 12.5% and glass parts is 15%. (Note: From September 1, color televisions from Thailand are imported duty free. End Note.) Electric fans receive a duty of 15%, while the import duty on the input, iron alloy coil, is 20%. The import duty on transmission assembly at 15% is the same as the import duty on its raw materials like bearing and rubber parts. Indian auto manufacturers have also complained that the bilateral FTAs threaten their future existence. The import duty on natural rubber, for instance, has remained unchanged at 20%, while the import duty on tires is 15% and even lower at 7.5% under the FTA with Sri Lanka. To correct this anomaly, the Prime Minister's Office has formed a "Committee on Inverted Duty Structure" under the chairmanship of Planning Commission Member Anwarul Hoda.

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More Trade for Me - Not For You  
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¶15. (SBU) Comment: While complaints about this inverted duty structure may have dampened enthusiasm for FTAs/RTAs, the Doha deadlock has led to greater GOI stress on bilateral and regional trade agreements, including a renewed push for greater market access in Southeast Asian countries and its immediate neighborhood. India sees good prospects in forging greater economic ties with Southeast Asia, Latin America and South Africa to bolster its growing foreign trade sector. Among these regions, Southeast Asia is the most advantageous for India in terms of cost-competitiveness.

¶16. (SBU) Comment Continued: However, recent experiences indicate that in bilateral/regional trade pacts, GOI trade negotiators tend to adopt an inherently inward-looking approach. Tariffs on products of interest to India's trading partners that might impact domestic producers are kept high, while products with low trade prospects are given primacy in drawing up free trade/"early harvest" lists. In addition, the non-tariff barriers and customs regulations that affect much of the trade in the northeast are a significant logistical barrier to accessing the Indian market. This is evident in India's restrictive trade agreements with its small neighbors like Bangladesh and Nepal - countries with little potential to disrupt the Indian domestic market. India's posturing in Geneva as defender of the least developed countries is belied by the meager terms it offers these same countries in trade negotiations.

JARDINE